Strategic Sourcing and Procurement of FM: New ISO standard and a case from practice.

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STRATEGIC SOURCING AND PROCUREMENT OF FM

NEW ISO STANDARD AND A CASE FROM PRACTICE

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Introduction

Decisions about sourcing are essential aspects of FM. There has been a considerable amount of debate and research about whether to outsource or not and how to do procurement and outsourcing. There has been less debate and research on how to conduct a strategic sourcing process leading to an informed decision between the different sourcing options.

Strategic sourcing is related to the classical corporate management question of making or buying. The question can be seen as a narrow and short term economical question of finding the cheapest solution, but it can also be regarded as a strategic issue, where long term benefits and risks are more in focus. As many organisations have achieved increased experience with outsourcing of FM, the strategic view seems to become more important. One sign of this is that a new international standard ISO 41012 (ISO, 2016), which originally aimed at updating the European standard EN 15221-2 (CEN, 2006) with guidance on making FM agreements, ended up also including guidance on strategic sourcing. The ISO standard includes a sourcing process with 10 main phases:

1. Sourcing strategy and core business context
2. Identify current and future needs
3. Translate needs into requirements
4. Describe the service levels
5. Identify service delivery options
6. Business case development
7. Select preferred sourcing/service delivery option
8. Facilities service provision
   - Internal service provision
   - External service provision
9. FM service procurement and FM-agreement
10. Measure service provision performance

This article investigates the process of strategic sourcing and procurement of FM based on a case study of the Danish Broadcasting Corporation (DR). The purpose it to provide insights into strategic sourcing concerning FM and how it can contribute to a sourcing decision that combines the benefits of internal and external provision with consideration of business risk and cost. The article also compares the practical case with the strategic sourcing process recommended in the ISO standard. Further information can be found in a scientific journal paper (Jensen, 2017).

The case

DR is an independent public institution financed by license fees and provides radio, television and online media services in Denmark and has about 3,000 employees. DR relocated its activities in the Copenhagen area from 12 former addresses to a new headquarters called DR Byen (DR City) in the period 2006-2009.

DR-Byen is a complex of approx. 132.000 m2, which includes a concert hall with public performances. Besides, DR has smaller facilities in provincial towns around Denmark.

DR has a long history of outsourcing FM services, see Figure 1. Before relocating to the new headquarters DR Byen, it was decided to make a comprehensive outsourcing of all cleaning and catering in a bundled contract with one provider for the period 2006-2010 resulting in substantial cost savings. In a next round of public tendering, it was decided to extend the contract much further to achieve maximum cost savings. Therefore, near enough all FM services became part of the scope; including for instance maintenance planning and technical building operation. The economic volume was more than the double compared to the former contract. The result was an integrated FM (I-FM) contract with a leading Scandinavian service provider with strong focus on I-FM contracts. The contract period was 5 years from 2011 to 2015. It was the largest I-FM contract made in Denmark at the time.

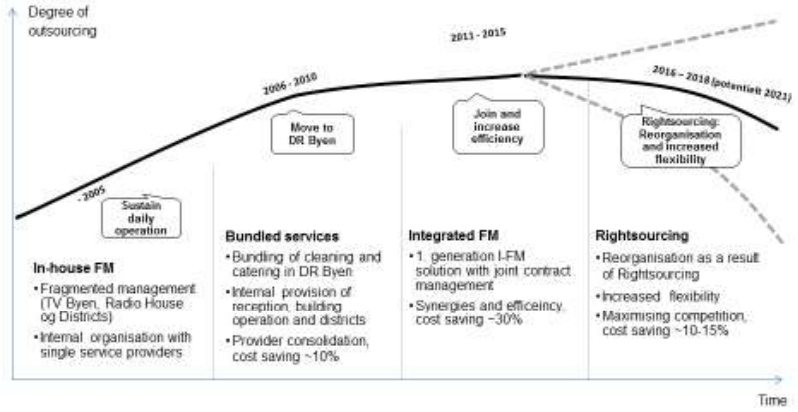

Figure 1: The history of outsourcing in DR (Source:DR)

DR's evaluation of the former I-FM collaboration

As a basis for starting the strategic sourcing process, leading up to a new procurement round in 2015, DR made a thorough evaluation in autumn 2013 of the ongoing I-FM collaboration. When the contract period started by 1 January 2011, most staff working under the former contract was transferred to the new provider as part of the transition. The first part of the contract period was an implementation process of the contract with the new provider, and DR faced many problems in getting a satisfactory service provision and collaboration with the new provider. It was almost half way during the contract period, before most trouble-shooting had been sorted out and a more development oriented phase directed towards optimising the service provision could start. After about three years in the contract period. preparation for contract termination started with monthly transition meetings between DR and the provider with the aim to retain staff, resolve disagreements and prepare time schedules.

Examples of specific problems in the implementation phase were that it took two years before DR got reasonable insight into the provider's plans for building maintenance and investments and it took three years before DR received satisfactory plans for preventive maintenance of the headquarters and proposals for energy optimisations. It was also discovered that the interphases between the providers IT systems and DR systems were much more complicated than expected; partly due to DR's policy for IT security. DR decided to use options to withdraw minor parts of the services from the contract, but it turned out to be more difficult than expected to change the contract, because the provider had integrated all the services in the contract in their central service centre system. DR's contract manager found that an I-FM provider was "too big to fail".

The contract included a main part with a fixed fee and other parts with payment per project or service order. The fixed fee was reduced with 1 million DKK per year (slightly more than 1%) over the contract period without reducing service quality. The provider was obliged to prepare a catalogue each year with proposals for such savings to be accepted by DR. From hindsight DR evaluates that they altogether achieved a saving of 20-30% by making the I-FM contract. Only about two thirds of the initial expected savings were achieved, but the savings were still substantial. It is DR's impression that the provider made a very low bid to get a better foothold on the Danish market with a large contract.

A major problem seen from DR's perspective was the technical building area. DR found that the provider did not have the relevant competences and resources on the overall strategic level to be sufficiently prepared for unexpected incidents in relation to building technic. There were some serious incidents during the contract period with cut out of electricity and cooling supply, which showed that the necessary people and competences in the providers' organisation were not in place. DR found that the provider had reduced the amount of staff in this area to an unacceptable level both on strategic and operational level.

Even though the I-FM collaboration in some areas has been unsatisfactory, there have also been many areas where it has worked well.
DR's contract manager reckons that there probably would have been similar problems, if they had chosen another I-FM provider. His reflection was, that when one focuses narrowly on getting cost reductions, you cannot expect to get a high service quality at the same time.

"Strategic sourcing is related to the classical corporate management question of making or buying"

The strategic sourcing process

DR defined the purpose of the strategic sourcing and procurement process as:

1. Make a thorough analysis of the FM area (including evaluating the present FM procurement to gain as much learning as possible for the new procurement)
2. Decide the optimal scope for the new procurement
3. Make new agreement(s), which ensure
   - a high degree of supply security
   - a satisfactory quality and service level
   - that the total economic frame for FM provision as far as possible is kept
   - that DR fulfil its legal obligation for public procurement on the area and that DR get the best possible agreement conditions

The whole process was divided in five phases with the following periods:

1. Planning and project establishing (September 2013 – February 2014)
2. Sourcing analysis (December 2013 – May 2014)
3. Preparing of tender material (March 2014 – November 2014)
4. Tendering process (August 2014 – October 2015)
5. Implementation and transition (October 2015 – June 2016)

The project group consisted of a project manager from DR Estates and Services and a person from the procurement unit in the financial department. The project group also involved an external consultant from the company fm3.dk specialised in FM consulting. A steering group was established and the project work involved the staff in DR Estates and Services as well as super users from a number of other departments in DR.

The strategic sourcing covered the second of the five phases. It should be noted that most of the following analysis is case-specific and should not be transferred to other cases without giving necessary considerations to the case-specific context and implications.

A fundamental part of the strategic sourcing analysis was to analyse each of 12 main service areas in relation to what the degree each service was evaluated in relation to the following seven criteria:

1. Is critical for DR's core business
2. Is strategic/tactical for DR
3. Influences the strategic/tactical FM
4. Insourcing would set requirement for DR's competences
5. Impacts DR's staff
6. Impacts DR's guest
7. Can devaluate DR's assets if not performed optimally

The results of the analysis were presented in a so-called right-sourcing matrix, where traffic lights showed, whether a service was evaluated high (red), medium (yellow) or low degree (green), see Figure 2. The service area 'building technic' stood out as the only one where all criteria were evaluated either high or medium.

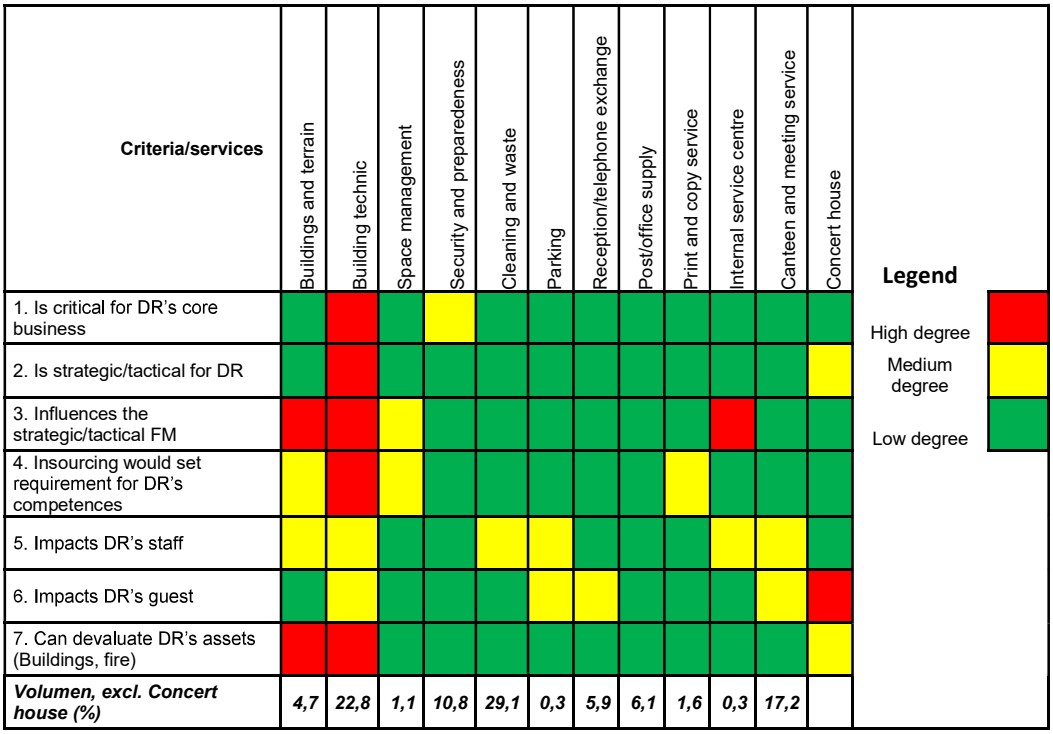

Figure 2: Right-sourcing matrix for FM services in DR (Source: DR, based on a template developed by Preben Gramstrup, fm3.dk)

Another element in the analysis of the different services was using a priority triangle to evaluate what was most important for each service in terms of the three criteria: User satisfaction, supply security, and economy. The service area 'cleaning and waste' stood out as having highest priority in relation to user satisfaction, while 'building technic' had highest priority in relation to supply security, and 'parking' was the service where economy had highest priority. The priority triangle was also used on a more detailed level to analyse, which aspect in relation to a specific service area had different priority concerning the same three criteria as part of defining the more specific requirements for the tender material.

The possibility to achieve synergies between different work processes by bundling different service areas was analysed from an 'inside-out' perspective by use of a proximity matrix similar to what is often used for space briefing to analyse proximity between different functions, areas or rooms, see Figure 3. In the matrix all service areas are listed both horizontally and vertically and traffic lights are used like in the right-sourcing matrix (except that only the boxes above or below the diagonal needs filling in due to symmetry). The results showed that synergies were mostly found between the service areas 'building and terrain', 'building technic', space management' and 'security and preparedness' and between the service areas 'reception/telephone exchange', 'internal service centre' and 'security and preparedness'.

All synergies were found to be connected to operational processes with a high degree of shared operational activities.

The analysis of bundling was supplemented by an 'outside-in' perspective as part of a market analysis, which applied a sourcing model developed by Krajlic (1983). This model is in its simplest form a 2 x 2 matrix with profit or value impact (low – high) for the company on one axis and market supply risk or complexity (low – high) on the other axis. Items with high impact and high risk are seen as strategic, where make or buy consideration should be in focus. Items with low impact and low risk are seen as non-critical, where product standardisation should be in focus. High impact combined with low risk is characterizing items suitable for leverage or competition with full exploitation of purchasing power with high requirements.

The last square with low impact and high risk is characterized as bottleneck, where control of vendors and back up plans should be considered. The analysis showed that most services were seen as non-critical and the only services in the strategic square were critical parts of 'building technic'.

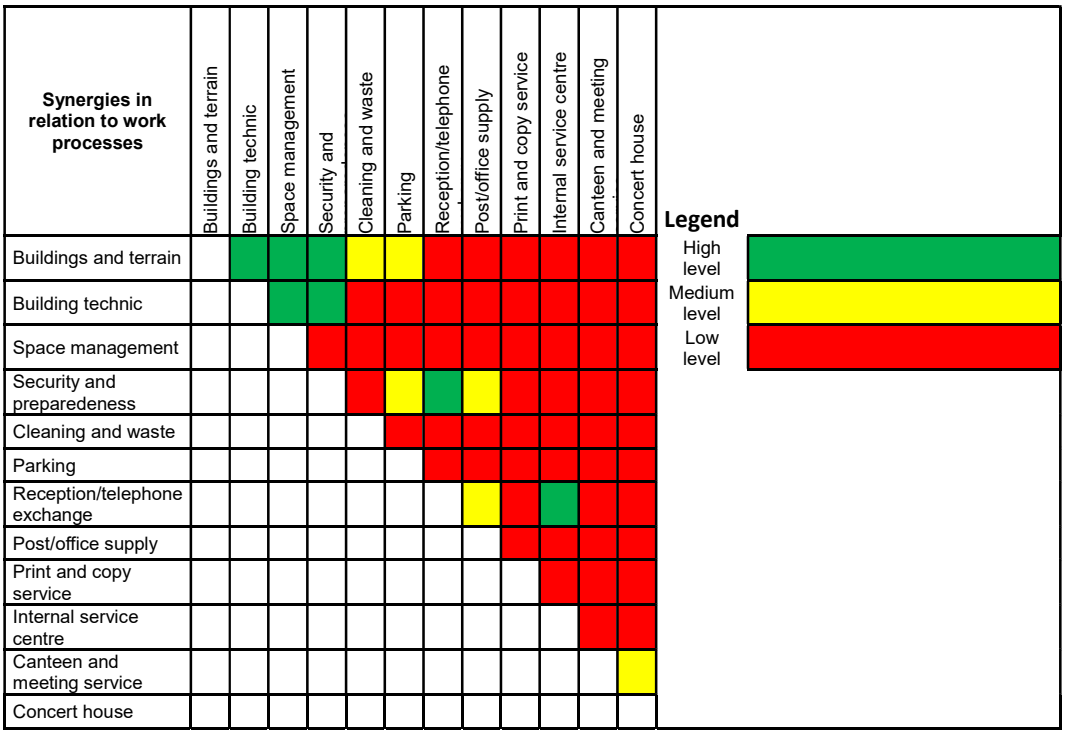

Figure 3: Synergies between work processes for FM services in DR (Source: DR and Preben Gramstrup, fm3.dk)

A detailed analysis was made to distinguish between critical and non-critical 'building technic'.

The market analysis also included meetings and consultations with a large number of companies and experts to collect knowledge about current market situation and experiences with different sourcing and procurement solutions seen from the demand and supply side as well as by independent observers. The market research also included an overview of potential providers presented in a provider matrix, showing which providers were likely to be able to offer the different bundles of services that the project group was recommending. This was done to check and verify that the recommended bundles would attract a sufficient number of potential tenderers to create the intended competition.

Sourcing models

The analysis defined the following 4 sourcing models:

- In-house/own production
- Singles services
- Bundled services
- I-FM

The models were compared according to a number of criteria see Figure 4.
All the models were regarded to be able to fulfil requirement concerning high user satisfaction, flexibility, possibility for benchmarking, and a simple and clear monitoring by KPI's. I-FM was evaluated problematic in relation to possibility to change provider and to create a transparent pricing model. In-house was evaluated as less optimal with regards to the same two criteria as well as concerning to keep within the economical frame. Single services were evaluated as less optimal with regards to a controlled implementation and security for supply of FM services. There were no reservations for any of criteria for bundled services. In relation to the size of the own FM organisation, it was evaluated to be big for in-house provision and small for I-FM and bundled services, while it for single services was evaluated as small/medium depending on number of actually single service providers.

The analysis was synthesized in the presentation and evaluation of 3 alternatives for scope of in-house versus outsourcing. The overall scope of FM was defined with a division in strategic, tactical and operational level.

The three alternatives were:

1. DR provides all FM services in-house
2. DR only provides the strategic tasks and a few of the tactical tasks, i.e. benchmarking and contract management

Sourcing model	Keep within the economical frame	High user satisfaction	Flexibility	Possibility for changing provider	Controlled implementation	Security for supply of FM	Transparent pricing model	Benchmarking	Simple and clear foolow-up by KPI's	Own FM organization
In-house/ own production										Large
Single services										Small/medium
Bundled services										Small
I-FM										Small

Figure 4: Sourcing models evaluated in DR's analysis. Green: Fulfilled; Yellow: Possible but not optimal; Red: Difficult to get fulfilled. (Source: DR and Preben Gramstrup, fm3.dk)

3. DR provide all strategic, tactical and the most important oprational task, i.e. service centre, building technic and property operation, and concert house

The project group evaluated the three alternatives in relation to the success criteria mentioned earlier. The result was a recommendation of alternative 3. Main arguments against alternative 1 were that the success criteria concerning economy and security for service provision could not be fulfilled and even though the internal FM organisation would be big, it would still not have sufficient critical mass for all service areas to be efficient. Main arguments against alternative 2 were that the success criteria concerning flexibility and possibility for continuous competition were not fulfilled and that DR would have a lack of control over data and not be able to proactively develop the FM area on their own. An important precondition for recommending alternative 3 was that DR established and managed their own helpdesk and service portal.

The result was a recommendation of a sourcing solution with a combination of insourcing, bundled outsourcing and single service outsourcing (out-tasking). The insourcing covered an economic volume of 9% of the I-FM contract and covered the tactical part of building operation as well as the operational functions: handyman, HVAC, and service portal.

The bundled services covered the main economic volume with 70% of the I-FM contract. The services were divided in 3 contracts: 'Catering', 'Security and internal service', and 'Cleaning'. Even though catering and cleaning could be regarded as single services, the contracts had large volumes and included many sub-services and all DR's locations for cleaning and the two main locations for catering.

The single services included 7 separate contracts together covering the remaining economic volume of 21% of the I-FM contract.

The single service contracts were 'Building technic' (only frequent and legal required inspections and service operations), 'Terrain', 'Pest control', 'Waste handling', 'Fruit provision', 'Office supplies' and 'Catering for commercial and larger events in concert house'.

Alongside the strategic sourcing analysis work with preparing the detailed tender specifications and definitions of SLA's and KPI's had started in the project group with involvement of a larger group of staff. The procurement process started with pre-qualifications in autumn 2014 and finished with tendering and contracting in the second half of 2015. The former I-FM terminated by the end of 2015, and the new contracts started by 1 January 2016.

The overall results of the sourcing and procurement process was that DR achieved a total cost reduction of 10-15%. This even though the insourced part of 'building technic' turned out to be more expensive than expected.

The strategic sourcing process compared with the new ISO-standard

Compared to the new standard ISO 41012, the main activities described in the standard can be identified in DR's strategic sourcing process. A main difference is that the standard takes the starting point more or less from a 'clean sheet', where you start the process from scratch without a prior history of FM sourcing.

This means that in DR's case many aspects did not need in-depth consideration, because of the organisation's history of outsourcing. The first two phases of investigating the sourcing strategy in relation to the core business context and identifying current and future needs mostly consisted of the evaluation of the ongoing I-FM collaboration.

Another difference was that the process in DR had less phases and more parallel activities in developing the sourcing and procurement strategy. This also relates to the most essential difference. The standard is based on a sequential process starting with a gradual specification of the demand and needs, before investigating possible delivery options. In the DR case, the delivery options were investigated, before making detailed specification of the needs in terms of Service Levels. This turned out to be crucial as the ways, needs are specified, are depending on the chosen sourcing models. For instance, the choice of an output based cleaning model meant that the service levels for cleaning needed to be specified in a completely different way compared to the former frequency based model.
The same was the case for catering with introduction of a new "restaurant" model compared to the former model based on a management fee.

"WHEN ONE FOCUSES NARROWLY ON GETTING COST REDUCTIONS, YOU CANNOT EXPECT TO GET A HIGH SERVICE QUALITY AT THE SAME TIME"

Conclusion

The case applies the concept of 'right-sourcing'. This is a concept mostly used by consultants and until now hardly used in scientific research. The internationally renowned IT-consulting company Gartner presents a toolkit for right-sourcing on their website with eight sourcing models and six sourcing options. An example of a definition from another company website (Blur Group) says: "Right-sourcing goes beyond outsourcing, ensuring that every core business function, including in-house and supply chain, is delivering maximum value to your organization, based on cost, quality, and expediency. Right-sourcing is finding the right team to do the job better, faster, and at the right price." The advantage of the concept is that it removes the discussion from the dichotomy between either outsourcing or in-house and opens up for a more nuanced discussion with the possibility to combine different sourcing solutions.

The case presented and analysed in this article shows the relevance of such a more nuanced approach. Based on a thorough analysis, the case organisation decided to change the sourcing strategy with insourcing of the most critical building related activities and changing the procurement strategy to 3 bundled service contracts and 7 single service contracts. The choice between outsourcing and insourcing was mainly based on a balance between cost and business risk and the choice between outsourcing versus out-tasking was mainly based on a balance between high economic volume and possibilities to obtain synergies to make contracts attractive by providers versus lowest possible management fee with a short value chain and direct access to service area experts. To get attractive offers you need to be an attractive client.

The comparison of the strategic sourcing process in the case organisation and the new ISO standard showed that the process in DR had less phases and more parallel activities in developing the sourcing and procurement strategy. The main problem with the standard is that it is based on a sequential model starting with detailing the demand and needs before investigating sourcing option. The case shows that the ways needs are specified in tender material are depending on the chosen sourcing models. Besides that, the standard has a sound approach to strategic sourcing being open to combining internal and external service provisions.

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